STATE OF CALIFORNIA PETE WILSON, *Governor*

PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

April 23, 1997

William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, N.W. , Room 222
Washington, D.C. 20036

Re: CC Docket No. 96-149

Dear Mr. Caton:

Enclosed you will find an original and sixteen copies of **REPLY COMMENTS OF THE STATE OF CALIFORNIA AND THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA IN CONNECTION WITH EXPEDITED RECONSIDERATION OF INTERPRETATION OF SECTION 272(e)(4).**

Also enclosed is one additional copy to be conformed and returned to me in the enclosed self-addressed envelope

Thank you for your attention to this matter. If you have any questions, please call me at (415) 703-2047.

Sincerely,

Ellen S. LeVine
Attorney for the People of the
State of California and the Public
Utilities Commission of the State
of California

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BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

FCC MAIL ROOM

APR 24 1997

In the Matter of	)	FCC 96-308
	)	
Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended;	)	CC Docket No. 96-149
	)	
and	)	
	)	
Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LECs' Local Exchange Area	)	

REPLY COMMENTS OF THE PEOPLE OF THE STATE OF CALIFORNIA AND THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA IN CONNECTION WITH EXPEDITED RECONSIDERATION OF INTERPRETATION OF SECTION 272(e)(4)

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April 23, 1997

I. INTRODUCTION

The People of the State of California and the Public Utilities Commission of the State of California ("California" or "CPUC") hereby respectfully submit these reply comments to the Federal Communications Commission ("FCC" or "Commission") on the Comments Requested in Connection with Expedited Reconsideration of Interpretation of Section 272(e)(4) regarding rules to implement, and, where necessary, to clarify the non-accounting separate affiliate and nondiscrimination safeguards prescribed by Congress in section 272 of the Telecommunications Act of 1996 ("the Act"). These safeguards are intended to protect subscribers to the Bell Operating Companies' ("BOCs'") monopoly services (such as local telephony) against the potential risk of having to pay costs incurred by BOCs to enter competitive services (such as interLATA services and equipment manufacturing). They also serve to protect new competitors from the BOCs' ability to use their existing market power in local exchange services to obtain an anticompetitive advantage in the new markets the BOCs now seek to enter. This rulemaking is issued pursuant to the Act.

II. SUMMARY

The CPUC does not share the BOCs' interpretation of the Act as it relates to the BOCs' provision of interLATA services in two respects. The Act first requires that the BOC satisfy the 271 checklist before providing in-region interLATA services. The Act secondly requires the implementation of both the structural and non-structural safeguards of section 272 pertaining to a BOC's provision of interLATA services. These conditions apply regardless of whether the services in question are classified as wholesale or as retail.

The Commission's First Report and Order correctly interpreted the requirements of sections 271, 272(a) and 272(e) of the Act regarding the BOCs' provision of interLATA services. California supports the Commission's conclusions that the BOCs lack in-region interLATA authority until the Commission determines that the BOCs have met the requirements of section 271. Thereafter, the BOCs must conduct their interLATA operations only through a separate affiliate as required by section 272 of the Act.

What the BOCs are proposing in their comments would negate the important safeguards of the Act. These safeguards address two important concerns: the prevention of cross-subsidization and the non-discriminatory treatment of affiliates. The Commission should reaffirm its earlier conclusion that section 272(e)(4) is not a grant of authority for a BOC to provide in-region interLATA services, including wholesale interLATA services.

III. DISCUSSION

A. Meaning of "Originate"

The FCC seeks comment on what it means to "originate" an interLATA telecommunications service. Pacific Bell has argued that its reading of section 272(e)(4) does not conflict with its reading of section 272 (a) because when a BOC provides in-region interLATA telecommunications service to its affiliate, it does not "originate" such services. (See Bell Company Comments, Executive Summary, p. 1.)

California does not agree with this interpretation. California believes that any call which originates within a BOC's service area must be considered as having "originated"

therein, regardless of whether the retail provider is the BOC, its section 272 affiliate, or another carrier. Indeed, section 271(b)(1), which broadly prohibits a BOC or its affiliate from providing interLATA services originating in any of its in-region States prior to FCC approval, also uses a form of the term "originate". This supports the Commission's interpretation of the meaning of the word "originate" as it relates to a BOC's provision of interLATA service.

Contrary to the BOCs' assertions, the Act did not eliminate the proscription on in-region interLATA services. The Act replaced the MFJ and, it provided in sections 271 and 272 the terms under which a BOC may enter the interLATA market. Until these terms are satisfied, the prohibition continues.

The MFJ ban on interLATA service was based on the BOCs' control of local exchange services. It had nothing to do with who makes a sale of an interLATA service. The Act, which supplants the MFJ, must be viewed within the same context. The Act addresses the question of the BOC's dominance over the local exchange market by providing that, upon fulfillment of the section 271 competitive checklist, a BOC may be authorized to provide interLATA services.

Despite the dawning of local exchange competition, the BOCs remain largely in control of the local exchange market. Thus, even though a BOC may not be the retail provider of interLATA services, for competitive analysis purposes, it is the controlling provider of local exchange access. For this reason, the BOC should be considered the "originator" of virtually all switched traffic in its service territory. Until a BOC meets the

requirements of sections 271 and 272, this fact should weigh heavily against the lifting of the MFJ-imposed ban on in-region interLATA services.

B. Wholesale vs. Retail Provision of InterLATA Services

The FCC asks whether the principal concerns that underlie the separate affiliate requirement of section 272 – discrimination and cost misallocation by a BOC – are less serious in the context of the wholesale provisioning of in-region interLATA services to affiliates than in the context of the direct retail provisioning of such services. California agrees with Ohio's comments, that these principal concerns are no less of a concern should the BOC be permitted to provide interLATA service on a wholesale basis. (Comments submitted by the Public Utilities Commission of Ohio, pp. 5-6.) Ohio's reasoning is that, "Without proper pre-authority scrutiny, there is a concern that local facilities that are currently used for local services, and paid for by local ratepayers will be used for long distance without proper cost allocation. Such a scenario would harm captive local customers and long-distance competition." (Id.)

California believes that, although discrimination may be less of an issue for wholesale services than for retail, the likelihood of cost misallocation and cross-subsidization of competitive services remains irrespective of the nature of the services. Specifically, the facilities that comprise the BOCs' Official Services Network are all above-the-line assets, and have therefore been included in regulated monopoly rates. Allowing the BOCs to provide interLATA wholesale services without a structural separation requirement creates an unacceptable level of risk that the expenditures associated with the wholesale long distance operation will be charged to local operations.

Such "cost-shifting" from competitive to monopoly services could have significant adverse consequences on both Universal Service and on competition. Congress anticipated this problem by instituting the separate affiliate requirements of section 272 (a).

The FCC asks what relevance, if any, is the fact that there was no exception to the interLATA services restriction contained in the MFJ for wholesale interLATA services provided on a non-discriminatory basis, or that there is presently no wholesale interLATA services exception to section 271's prohibition on the provision of in-region interLATA services prior to FCC approval. Ohio correctly notes that section 271(a) must be understood to include all interLATA services that are not included in the exceptions directly referred to in 271(a). (Id.). Section 271 takes the trouble to list specific exceptions to the broad prohibition of section 271(a), yet it does not mention the wholesale provision of interLATA services as an exception. When Congress meant to exempt an interLATA service from the requirements of section 271(a), it explicitly said so. Failure to exempt wholesale interLATA services is a strong indication of Congress' intent not to exempt such services.

The legislative history of section 272(e)(4) corroborates Ohio's interpretation. The Text and Conference Report of the Act provides no support for the BOCs' contention of interLATA wholesale authority under section 272(e)(4). The Senate bill outlined the services that required structural separation as well as the specific exceptions to that requirement:

> The activities that must be separated from the entity providing telephone exchange service include

> telecommunications equipment manufacturing and interLATA telecommunications services, except out-of-region and incidental services (not including information services) and interLATA services that have been authorized by the MFJ court. A BOC also would have to provide alarm monitoring services and certain information services thorough a separate subsidiary, including cable services and information services which the company was not permitted to offer before July 24, 1991. In a related provision, section 203 of the bill provides that a BOC need not use a separate affiliate to provide video programming services over a common carrier video platform if it complies with certain obligations. (Text and Conference Report Summary, Volume 1, p. 150.)

The Senate Bill would also have allowed the FCC to grant exceptions to the separate subsidiary requirement, but only after the BOC had fulfilled the competitive checklist (known under the Act as Sec. 271):

> New subsection 252(h) provides that the Commission may grant exceptions to the requirements of section 252 upon a showing that granting of such exception is necessary for the public interest, convenience, and necessity. The Senate intends this exception authority to be used whenever a requirement of this section is not necessary to protect consumers or to prevent anti-competitive behavior. However, the Senate does <u>not</u> intend that the Commission would grant an exception to the basic separate subsidiary requirements of this section for <u>any</u> service prior to authorizing the provision of interLATA service under section 255 by the BOC seeking the exception to Telecommunications Act of 1996 requirement of this section. (<u>Id</u>., p. 151, emphasis added.)

The House amendment also required structural separation for the BOC's long distance subsidiary:

The Conference agreement adopted the Senate provisions with several modifications. Most notably, the Conference Committee specifically deleted the FCC's ability to grant exceptions to the separate subsidiary requirement:

> The conferees deleted the Senate provision providing for Commission exceptions to the requirements of this section. Instead, the conferees adopted a three year "sunset" of the separate affiliate requirement for interLATA services and manufacturing activities. The three year period commences on the date on which the BOC is authorized to offer interLATA services. In addition, the conference agreement provides that the separate affiliate requirement for interLATA information services "sunsets" four years after the date of enactment of the Telecommunications Act of 1996.
>
> In any case, the Commission is given authority to extend the separate affiliate requirement by rule or order. (Id., p. 152, emphasis added.)

From the foregoing, it can be noted that neither the Senate, House, nor Conference Committee versions of the bill exempted the wholesale provision of interLATA service from the requirements of sections 271 and 272 (a). Congress provided no exceptions beyond those explicitly mentioned in the Act. Indeed, the final version of the bill deleted the Senate provision that would have allowed the Commission to make exceptions to section 272(a) on a case-by-case basis. The BOCs have no legal basis under the Act to provide wholesale interLATA services under section 272(e)(4).

C. Meaning of "InterLATA Services" in Section 272(e)(4).

Section 272(e)(4) states that "a BOC and an affiliate that is subject to the requirements of section 251(c) may provide any interLATA or intraLATA facilities or services to its interLATA affiliate." The BOCs have essentially interpreted this passage as a lifting of the ban on wholesale interLATA services. California believes that the BOCs have misinterpreted the meaning of this section. California believes Congress intended that section 272(e)(4)'s use of the terms "interLATA or intraLATA facilities or

services" refers to the provision of the respective types of access – inter- and intraLATA – that the BOCs have always provided. This interpretation conforms section 272(e)(4) with sections 271, and 272 (a).

IV. CONCLUSION

The Commission should affirm its earlier conclusion that section 272(e)(4) is not a grant of authority for a BOC to provide interLATA services, including wholesale interLATA services provided to its interLATA affiliate. In order to provide such

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services, a BOC must satisfy the competitive checklist of section 271(a) and receive Commission authorization. Thereafter, section 272 of the Act requires that all interLATA operations be conducted through a separate affiliate.

Dated: April 23, 1997

Respectfully submitted,

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Certificate of Service

I, Nancy A. Salyer, hereby certify that on this 23rd day of April, 1997, a true and correct copy of the foregoing Reply Comments of the People of the State of California And the Public Utilities Commission of the State of California In Connection with Expedited Reconsideration of Interpretation of Section 272(e)(4) in FCC 96-308, CC Docket No. 96-149, was mailed first class, postage prepaid to all known parties of record.

Nancy A. Salyer